

## SUBCOMMITTEE NO. 4

## Agenda

Michael Machado, Chair  
Robert Dutton  
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### Agenda – Part “A”

Tuesday, May 22, 2007  
10:00 a.m.  
Room 2040

Consultant: Brian Annis

### May Revision & Open Issues

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**Departments with Budget Issues Proposed for Consent / Vote Only****2740 Department of Motor Vehicles**

1. **Additional Vendor Costs for Electronic Insurance Verification (May Finance Letter #7).** The Department of Motor Vehicles (DMV) requests \$9.4 million (various special funds) to pay increased vendor costs for the Vehicle Registration Financial Responsibility Program (Program) due to higher-than-anticipated activity. Budgeted Program costs would increase from \$13.1 million to \$22.5 million. The Program was established by Chapter 920, Statutes of 2004 (SB 1500) and requires insurance companies to electronically report insurance policies on private-use vehicles and the DMV to suspend vehicle registrations when evidence of insurance is not provided by specified deadlines. The Program reduces the number of uninsured drivers, and should result in state Medi-Cal savings (to the extent that Medi-Cal recipients are involved in accidents and private auto insurance can cover the related healthcare costs). Costs are up because the vendor is paid per transaction and suspension notices are expected to be sent for 5.5 million vehicles lacking proof of insurance rather than the 3.6 million previously anticipated. The current vendor contract ends in 2 years, the DMV may submit a budget change proposal in the 2008-09 Governor's budget to either bring the activity in-house or continue contracting out after a new procurement.

**Staff Recommendation:** Approve the May Finance Letter.

2. **Telephone Service Center (May Finance Letter #8).** The Administration requests a budget reduction of \$826,000 (various special funds) and a current-year reversion of \$2.8 million due to savings related to the decision to use the CalNet II contractor for replacement of the DMV's telephone service center equipment, an option which was not available at the time the Feasibility Study Report and funding was approved last year. The CalNet II contract was finalized by the Department of Technology Services on January 31, 2007. Under the CalNet II contract, vendors own the telephony equipment and software. DMV estimates that using CalNet II, instead of proceeding with the original project approved last year, will save the state \$7 million over the life of the project (reducing total costs from \$31.9 million to \$24.9 million).

**Staff Recommendation:** Approve the May Finance Letter.

- 3. Web Site Infrastructure (WSI) Project Reappropriation (Administration Request).** The Administration requests the re-appropriation of the unencumbered balance of \$11,867,233 for the Web Site Infrastructure (WSI) Project originally funded in the 2006 Budget Act. This re-appropriation is due to a change in the bid due date and the contract award date by the Department of General Services (DGS). During the bid evaluation review, DGS declared the WSI bids for the hardware, software, and contract services to be second drafts and extended the final bid due date to July 26, 2007. The project will allow DMV to expand services on the web while adding additional layers of security. The DMV and the Department of Finance requested this change by phone and email on Tuesday, May 15. The Administration indicated the DGS decision was not known until after the May Letters were finalized.

**Staff Recommendation:** Approve a reappropriation for the Web Site Infrastructure project.

### **8380 Department of Personnel Administration**

- 4. Human Resources Modernization Project (April Finance Letter #1).** The Department of Personnel Administration (DPA) requests \$2.8 million (General Fund), 5.0 new positions, and 70 redirected/loaned positions, to begin development and design for the Human Resources (HR) Modernization Project. This proposal was discussed at the April 25 hearing and left open for further review and consideration of legislative reporting requirements. The LAO has developed the following Supplemental Reporting Language (SRL) in coordination with the DPA, the Department of Finance, the State Personnel Board and Committee staff:

**Supplemental Report Language:** *On or before February 5, 2008, the Department of Personnel Administration (DPA) shall submit an annual report concerning the Human Resources Modernization Project. The report will describe: (1) key activities of the project to date during 2007-08, (2) major planned and proposed activities of the project for the remainder of 2007-08 and 2008-09, (3) any significant changes in the plans, goals, or timelines for the project, and (4) any changes in the anticipated long-term costs of the project. The DPA shall consult with the executive officer of the State Personnel Board (SPB) or her designee in preparing the report, and the executive officer or her designee may include with the report a letter describing any areas of significant disagreement between SPB and the administration concerning the progress and plans of the project. Should the administration submit a budget change proposal (BCP) concerning the project to the Legislature as part of the 2008-09 Governor's Budget, the BCP may be designated as the submission satisfying this annual report requirement, provided that it includes all of the information described in this section.*

**Staff Recommendation:** Approve the Finance Letter with the addition of the LAO Supplemental Report Language.

**5. “Head Hunter” Services for Medical Classifications (April Finance Letter #2).**

The Department requests \$1.0 million (two-year limited term General Fund) to hire a recruitment contractor to locate and develop a pool of prospective healthcare professionals to fill State jobs at the California Department of Corrections and Rehabilitation, the Department of Mental Health, the Department of Developmental Services, and the Department of Veterans Affairs. This proposal was discussed at the April 25 hearing and left open for further review and consideration of performance-based contracting and appropriate funding levels. The LAO has developed the following compromise proposal in coordination with the DPA, the Department of Finance, and Committee staff: Reduce budgeted funding to \$350,000 in 2007-08 and \$350,000 in 2008-09, and add the following provisional language in DPA's budget item that would allow expenditures to increase up to \$1.5 million in each year, if specified requirements are met:

***Budget Bill Language:*** (X) Of the funds appropriated in this item, \$350,000 may be spent by the Department of Personnel Administration to contract with one or more recruitment contractors to locate and develop a pool of prospective health care professionals for various state departments that employ medical, mental health, and/or dental professionals. It is the intent of the Legislature that these contracts will be structured on a performance basis with payments tied to the successful hiring of state staff. Should the Director of Finance, upon receiving a recommendation of the Director of the Department of Personnel Administration, determine that it would be in the interests of the state to expand the dollar amount committed to this project, he may submit to the Chairperson of the Joint Legislative Budget Committee and the Legislative Analyst a report describing the number of individuals that have been successfully hired to permanent positions in affected departments as a result of the recruitment contractors' work to date and the anticipated benefits (including funds that affected departments would revert to the treasury due to decreased overtime and contracted personnel costs) that would result from an expansion of the funds committed to this project. Not less than 30 days after submitting the report described above, the Director of Finance may augment this item by an amount not exceeding \$1,500,000 in order to increase health care personnel recruitment efforts.

**Staff Recommendation:** Consistent with the LAO recommendation, reduce the requested funding from \$1.0 million to \$350,000 and adopt the LAO budget bill language.

- 6. Vacant Position Eliminations.** The Chair of the Budget Committee requests that Government Code 12439 be amended to require the abolishment of positions vacant for any twelve-month period, as specified. At present, GC 12439 requires the abolishment of positions when vacant for six consecutive months.

The Chair believes that, in the current state civil service environment, it has become increasingly rare that positions can be filled within the six month period of time. This leads to a loss of numerous positions that need to be reinstated and the beginning of the civil service cycle again. This problem has been prevalent in the area of hiring non-correctional personnel. This, among many other issues, has lead DPA to begin a top-to-bottom review of the whole state hiring process.

**Staff Recommendation:** Approved placeholder trailer bill language to require the abolishment of positions vacant for any twelve-month period, instead of the current six-month period.

## **9800 Augmentation for Employee Compensation**

- 7. Administration Budget Adjustments (January 19 Finance Letter):** The Administration requests the following budget changes related to a court decision in a suit brought by the California Correctional Peace Officer Association (CCPOA). The Finance Letter adds costs above the Governor's budget of \$153.5 million in 2006-07, and \$46.3 million in 2007-08, both General Fund. The total lawsuit costs through 2007-08 are \$439.8 million which is \$199.8 million more than assumed in the Governor's budget (all General Fund over 2006-07 and 2007-08). This issue was discussed at the April 25 hearing, but no budget action was taken pending receipt of the anticipated May Finance Letter.

**Staff Recommendation:** Approve the January 19 Finance Letter.

- 8. Administration Budget Adjustments (May Revision Finance Letter).** The Administration requests various changes in the employee compensation budget that net to a \$27.1 million increase in the General Fund cost and a \$2.1 million decrease to other funds. All of these changes are driven by updated estimates of the cost for current contractual obligations. The Adjustments include a Cost-of-Living Adjustment (COLA) of 3.4 percent instead of 3.3 percent (as estimated in the Governor's Budget); cost changes for Highway Patrol Officers and Engineers based on salary surveys of other public sector employers (again, per contractual terms); adjustments for updated population counts; and a reduction to the healthcare inflation cost from 12 percent to 10 percent based on the California Public Employees Retirement Board's decision to increase co-payments for office visits.

**Staff Recommendation:** Approve the funding adjustments requested in the May Finance Letter.

## Control Section 3.60 Contributions to Public Employees' Retirement Benefits

**9. Retirement Contribution Rates (PERS Action and May Finance Letter)** At the May 15, 2007, California Public Employees' Retirement System (PERS) Board hearing, the Board adopted revised State retirement contribution rates for 2007-08. According to estimates from the Department of Finance, the new rates will result in an increased cost of \$1.1 million General Fund and a decreased cost of \$23.0 million in other funds, relative to the amounts included in the Governor's Budget. The January Governor's Budget estimated contributions to PERS in 2007-08 at \$2.8 billion (\$1.5 billion General Fund) – an increase of \$80 million over 2006-07 (including a \$44 million General Fund increase). The Subcommittee previously discussed this issue (minus the May Revision adjustment) at the April 25 hearing.

**Background / Detail:** Control Section 3.60 of the budget bill specifies the contribution rates for the various retirement classes of State employees in CalPERS. This Control Section also authorizes the Department of Finance to adjust any appropriation in the budget bill as required to conform to changes in these rates. The Department of Finance also requests that the General Fund be decreased by \$272,000 to reflect the change to the State's fourth quarter deferral payment to PERS.

Category	Governor's Budget	New Rates
Miscellaneous, First Tier	16.997%	16.633%
Miscellaneous, Second Tier	16.778%	16.565%
State Industrial	17.861%	17.345%
State Safety	19.294%	18.835%
Highway Patrol	31.463%	32.212%
Peace Officer / Firefighter	24.505%	25.552%

**LAO Recommendation:** The Legislative Analyst recommends approval of the new rates and associated May Finance Letter.

**Staff Recommendation:** Approve the Control Section with the new rates adopted by the PERS Board and the related budget adjustments requested in the May Finance Letter.

**10. Pension Obligation Bonds.** (May Finance Letter) The Governor's Budget assumed that pension obligation bonds (POBs) will be sold in 2007-08, yielding \$525 million in General Fund benefit. The sale of these bonds has been delayed due to ongoing litigation. The May Finance Letter indicates that it now appears unlikely that there will be a final unappealable decision on the validity of the bonds in time for the bonds to offset the State's pension contributions in 2007-08, and requests to move the bond revenue from 2007-08 to 2008-09.

**Background / Detail:** In 2004, the Legislature enacted a law authorizing the sale of up to \$2 billion in POBs to fund the State's CalPERS obligation. Litigation has delayed the issuance of bonds and the Administration has reduced the assumed bond proceeds: the 2005 Budget Act assumed bond proceeds of \$525 million from a 2005-06 issuance; the 2006 Budget Act assumed no bond sales would occur in either 2005-06 or 2006-07, but assumed a bond issuance in 2007-08. A 2007-08 bond issuance totaling \$525 million was included in this year's Governor's Budget for 2007-08. The Administration is currently appealing a November 2005 Sacramento Superior Court decision that found the bonds unconstitutional. The practical effect of a delay in bond issuance beyond 2007-08 is a reduction to the General Fund reserve of \$525 million.

**LAO Recommendation:** The Legislative Analyst recommends approval of the May Finance Letter to shift POB funds out of 2007-08.

**Staff Recommendation:** Approve the May Finance Letter.

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**Staff Recommendation:** Approve the Staff Recommendation for each vote only issue as specified.

## Department Budgets Proposed for Discussion

### 1111 Bureau of Private Postsecondary and Vocational Education

The Bureau of Private Postsecondary and Vocational Education (BPPVE) is responsible for overseeing and approving private postsecondary vocational and degree-granting institutions to ensure they meet specified minimum statutory standards of quality education, fiscal requirements, and student protection. Under current law, the Bureau sunsets on July 1, 2007.

The Governor's Budget proposes expenditures of \$11.4 million (no General Fund) and 74.7 positions for the Bureau – an increase of \$3.0 million and 20.3 positions from adjusted 2006-07 expenditures.

#### Discussion / Vote Issues:

#### 1. Sunset of Bureau / Legislation to Recreate the Bureau (May Finance Letter):

The Administration requests a reduction of \$3.5 million to more-accurately reflect costs in 2007-08. Expenditure of the appropriation is contingent on policy legislation being enacted in 2007 to recreate the Bureau in statute after its July 1, 2007, sunset.

**Background / Detail:** Efforts to reform the Bureau and/or extend the sunset for the Bureau were unsuccessful in 2006. The Governor vetoed AB 2810, which would have extended the sunset to July 1, 2008, indicating that that measure did not include any reforms. Because the Bureau sunsets on July 1, 2007, and the Constitution prohibits the creation of a new office with urgency legislation (Article 4, Section 8), the Bureau cannot be extended, or recreated, until January 1, 2008.

Two policy bills currently under consideration, SB 823 (Perata) and AB 1525 (Cook) would respectively recreate the Bureau as the Board for Private Postsecondary Education on January 1, 2008, and provide for some student protections in the interim period of July 1, 2007, through December 31, 2007.

**Staff Recommendation:** Approve the Finance Letter, but also amend the Budget Bill to conform to SB 823. To conform to the bill, the three BPPVE appropriations should be changed from the "Bureau" organization code to the "Board" organizational code and the name changed to "Board of Private Postsecondary Education." The following budget bill language should be added:

*It is the intent of the Legislature to enact legislation in the first year of the 2007-08 Regular Session to establish the Board for Private Postsecondary Education effective January 1, 2008. Upon the effective date of legislation to establish the Board for Private Postsecondary Education, the Director of Finance may adjust this budget item, as necessary, to conform to the implementing legislation.*



## **1920 State Teachers' Retirement System**

The State Teachers' Retirement System (STRS) administers retirement and health benefits for more than 735,000 active and retired educators in the public schools from kindergarten through the community college system.

The State funds teachers' retirement based on two statutory formulas:

- **Benefits Funding** – the State's contribution is statutorily based on 2.017 percent of the teachers' salaries. The 2007-08 cost is budgeted at \$501 million General Fund.
- **Supplemental Benefit Maintenance Account (SBMA)** – The State's contribution is fixed by statute at 2.5 percent of teachers' salaries and is intended to provide retiree purchasing power protection. The Governor proposes statutory changes to vest purchasing power protection at 80 percent of initial retirement level, which the Department of Finance believes would result in a State savings of \$75 million and a revised contribution of \$547 million or 2.2 percent of salaries. (See issue #2 below for additional detail).

### **Issue Proposed for Vote Only:**

- 1. Reappropriation Request (May Finance Letter).** The Administration requests a reappropriation of up to \$3,476,000, which is 3 percent of Item 1920-001-0835, Budget Act of 2006. This reappropriation would allow CalSTRS to meet unanticipated system costs and promote better services to the system's membership. Budget bill language is also proposed to require quarterly reports to the Legislature on expenditures made pursuant to this item. The proposed language and methodology is consistent with a reappropriation item in the Budget Act of 2006.

**Staff Recommendation:** Approve this request.

### **Issue Proposed for Discussion and Vote:**

- 2. New Purchasing-Power-Protection Vesting & Related Savings (Governor's Budget Trailer Bill).** The proposed budget reduces the Supplemental Benefit Maintenance Account (SBMA) State contribution from 2.5 percent of salary to 2.2 percent – for an annual estimated savings of about \$75 million (from reducing this contribution from \$622 million to \$547 million). The Administration indicates that this contribution level is sufficient to maintain the existing purchasing-power-protection benefit based on a 2005 actuarial analysis. In return, the Administration proposes to vest this purchasing-power-protection benefit at 80-percent of an individual's initial retirement allowance (instead of the current vesting that sets the States contribution at 2.5 percent of salary without a specific level of purchasing-power-protection). Because the funding cut would be tied to a new vested benefit, the Administration argues this proposal is substantially different from the 2003-04 suspension currently under litigation.

**Background / Detail:** As actuarial analyses are performed over time, the State would have to pay more or less than 2.2 percent of salary – whatever was estimated as necessary to maintain the 80 percent purchasing power protection. However, the proposed trailer bill language cites 2.2 percent specifically instead of the amount needed to maintain the 80 percent benefit – so further statutory change would likely be needed if the contribution level necessary to maintain the new vested benefit changed from 2.2 percent.

**LAO Recommendation:** The Legislative Analyst recommends that the Legislature reject the Administration's proposal. The LAO finds there are risks in creating a new vested benefit, because under certain inflation assumptions, this proposal could increase State costs over the long-term (instead of producing the annual savings of about \$75 million as the Administration calculates). Additionally, the LAO recommends that any benefit changes be made in concert with a comprehensive plan to address retiree pension and health costs.

**Staff Comment:** STRS contracted for an actuarial analysis that estimates the Governor's proposal has a 68 percent chance of saving the State money, and a 32 percent chance of increasing State costs. Inflation rates exceeding 3.5 percent over a period of years would likely trigger State costs instead of savings. It should also be noted that STRS or other interested parties could choose to litigate the proposed change if they believed the new vesting was not a comparable benefit to the current statutory funding of 2.5 percent of salary.

The Assembly approved this proposal as budgeted, but indicated a desire to continue the discussion in Conference. Staff concurs and the following Staff Recommendation would put this issue into the Conference Committee.

**Staff Recommendation:** Reject the Administration's trailer bill, but retain the scored savings of \$75 million General Fund. This action will put the issue into the Budget Conference Committee.

## **1900 Public Employees' Retirement System**

The Public Employees' Retirement System (PERS) provides benefits to about one million active and inactive members and about 441,000 retirees. PERS membership is divided approximately in thirds among current and retired employees of the State, schools, and participating public agencies. The Constitution grants the PERS Board "plenary authority and fiduciary responsibility for investments of moneys and administration of the system" as specified. PERS was previously heard by the Subcommittee at the April 25 hearing, but the budget was left open pending expected May Revision Finance Letters.

### **Issue Proposed for Consent / Vote Only**

- 1. Final PERS Board Budget (May Finance Letter).** Consistent with the practice established last year, the Administration has submitted a May Revision Finance Letter to adjust the PERS budget to correspond to the final budget adopted by the PERS Board at the April 18 meeting. The items proposed for changes are "non-add" items displayed for informational purposes in the Budget Bill. The adjustments total an increase of \$42.4 million, and with April Finance Letter requests already approved, result in a total state operations budget of \$313 million.

**Staff Recommendation:** Approve the May Finance Letter.

### **Issue Proposed for Discussion / Vote**

- 2. Health Care Premium Report (May Finance Letter).** The Administration proposes that provisional language be added to Item 1900-001-0950 requiring PERS to report when it imposes health care premium increases on the state government, state workers, and state retirees that exceed actuarial assumptions listed in retiree health liability valuations that are expected to be produced by the State Controller's Office (SCO) on an ongoing basis. In its first actuarial valuation, released on May 7, 2007, the SCO used actuarial assumptions consistent with those specified by PERS, including estimates of future healthcare costs. The valuation assumes that the annual growth rate of health care premiums adopted by the CalPERS board will be 10 percent in 2008, 9.5 percent in 2009, and 9 percent in 2010, declining further until the annual rate of increase is no more than 4.5 percent per year beginning in 2017. The total cost of the State's unfunded liability was estimated at \$48 billion, and the costs to begin pre-funding this benefit was estimated at an additional \$1.2 billion annually.

**LAO Recommendation:** The Legislative Analyst believes additional reporting language is appropriate, given the significant degree of latitude currently granted PERS under state law to impose health premium increases on state and local governments, workers, and retirees. To ensure accurate and specific reporting consistent with the administration's intent, the LAO recommends the adoption of the following substitute provisional language:

*(X) Consistent with the statutory duty of the California Public Employees' Retirement System's health care program to promote increased economy and efficiency in state service, as described in Section 22751 of the Government Code, the Legislature finds and declares that the system is accountable to its members, governmental entities, and taxpayers with respect to the health premium increases that it imposes on public employers, public employees, and retirees. Within 45 days of adopting annual health care premium increases in excess of those assumed in the most recent actuarial valuation report for the State of California Retiree Health Benefits Program, the Board of Administration of the California Public Employees' Retirement System shall submit a report to the Chair of the Joint Legislative Budget Committee, the chairs of policy committees and budget subcommittees that consider the system's budget and activities, the Director of Finance, and the Legislative Analyst discussing specific actions that the system plans to take to ensure that future health care premium increases are at or below the levels assumed in the valuation report. This reporting requirement shall apply to any premium increases exceeding actuarial assumptions that are adopted for the 2008 calendar year, as well as any such increases adopted thereafter.*

**Staff Comment:** At a recent Assembly hearing, PERS staff indicated concern with the language, indicating that the actuarial assumptions were not intended to be a goal-setting device. The Assembly Subcommittee rejected the proposed language sharing the same concern as PERS staff.

There will likely be extensive discussions next year concerning post retirement benefits. Executive Order S-25-06 signed on December 28, 2006, created the Public Employee Post-Employment Benefits Commission to examine unfunded retirement benefits. This Commission is charged with delivering a plan by January 1, 2008, that would include a proposal to address the government's unfunded retiree health and pension obligations. As another input for those discussions, it would be valuable to know how contractual costs for 2008 compare to the actuarial assumptions in the Controller's study, and if PERS believes they can stay within the costs assumed in the actuarial study – this would be useful information to the Legislature when budget decisions are made in this area.

Additional edits may be warranted to the proposed language to address the concerns of PERS and the Assembly, but since the Assembly has already rejected this proposal Senate approval would send it to Conference. It may be more beneficial to amend the language at Conference Committee after further discussions with the Assembly and other interested parties have occurred.

**Staff Recommendation:** Approve the LAO's modified language to send the issue to Conference where further language edits may be warranted.

## **9650 Health and Dental Benefits for Annuitants**

This budget item provides funding for health and dental benefit services for more than 210,000 retired state employees and their dependents.

### **Discussion / Vote Issues:**

- 1. Budgeting for Retiree Health (Governor's Budget & May Revision).** The Governor's Budget included a total of \$1.137 billion for retiree health in 2007-08 (\$1.057 billion in the 9650 budget item and \$80 million in a special set-aside expenditure item). The LAO indicates that this 12 percent budget increase, over 2006-07, is less than the 14 percent average increase experienced over the past three years, and is less than the 16 percent average increase experienced over the last seven years.

The May Revision Letter requests to: shift the \$80 million in the set-aside item to the main 9650 item (for no net change in General Fund cost); reduce funding by \$9.5 million to match new premium estimates from the Department of Finance that relate to PERS staff recommendations to increase co-payments; and increase funding by \$2.9 million to account for recent enrollment increases.

**LAO Recommendation:** The Legislative Analyst recommends the Subcommittee takes action to put this budget item into the Conference Committee. The LAO indicates that the administration has provided less information than in the past on the reasoning and detailed estimates underlying its budget proposal for Item 9650, and questions if the revised amount in Item 9650 covers all likely budget-year costs, including enrollment growth.

**Staff Comment:** The PERS Board acted on May 15 on their staffs' recommendations to increase co-payments – the Board adopted some, but not all of the co-payment increases. Therefore, the Finance May Revision adjustment for co-payment increases does not tie to the final Board action. Staff understands that the Administration is working with CalPERS to adjust the savings assumptions in the May Revision.

**Staff Recommendation:** Approve the May Finance letter, but put the issue into Conference by adjusting each 9650 appropriation down by \$1,000. There will likely be further adjustments needed after the savings estimates are adjusted for final Board action on co-payments, and it is possible PERS will conclude negotiations with health plans, when the issue is open in Conference.

- 2. Medicare Part D Revenue (Governor's Budget):** As indicated on previous pages, the Governor's Budget assumes \$38.0 million in federal government reimbursements associated with Medicare Part D, which is the new prescription drug benefit. The Administration proposes that the State continue to receive these reimbursements and that the funds be used to offset the State's retiree healthcare costs.

**Background / Detail:** The federal Medicare Modernization Act was signed into law in December 2003 and established Medicare Part D. The Part D benefit is designed to provide Medicare beneficiaries with affordable drug coverage. The federal government created the Part D subsidies to encourage employers, such as the State, to continue offering drug benefits to retirees, instead of shifting enrollees to the Medicare plan. The California Legislature adopted AB 587 (Ch. 527, St. of 2005, Negrete McLeod) which requires CalPERS health program participants who are eligible to participate in Medicare Part D to enroll only in a CalPERS health plan.

**2006 Budget Act - Budget Bill Language:** In the spring of 2006, the CalPERS Board considered alternatives to using Part D reimbursements to offset State costs, including using the funding to lower costs for CalPERS enrollees and/or directing the Part D subsidies to the health plans instead of to the State. In response, the Legislature added budget bill language to direct the Part D reimbursements to a special deposit account with the intent that this would retain legislative oversight over the use of the funds. However, CalPERS obtained an opinion from the Attorney General that says the Part D funds should be deposited in the Contingency Reserve Fund (instead of the stand-alone special deposit fund that would segregate the funding until a new appropriation is provided).

**Staff Comment:** In past budgets, PERS has been able to provide some General Fund relief while also maintaining existing benefit levels. In 2005, PERS adopted a rate stabilization plan to spread market value asset gains and losses over 15 years instead of 3 years. While that change will be cost neutral over the long term, it did stabilize State costs and resulted in a General Fund savings of \$150 million in 2005-06. The Governor's proposal would seem to present PERS with a similar opportunity – to maintain existing benefit levels, while still aiding the General Fund with a \$38 million benefit.

**LAO Recommendation:** The Legislative Analyst recommends that the Legislature approve the Administration's proposal to use the Part D reimbursements to offset State costs, instead of to increase benefits or costs to state retirees. The LAO indicates this direction is consistent with the intent of both federal and State law. The LAO recommends technical language changes in conformance with this recommendation.

**Staff Recommendation:** Approve the Administration's proposal to use Part D to offset state costs, but direct staff to draft technical language changes pursuant to the LAO recommendation.

## 2180 Department of Corporations

The Department of Corporations (Corporations) administers and enforces State laws regulating securities, franchise investment, lenders, and certain fiduciaries. The Governor's January Budget proposed total expenditures of \$33.9 million (no General Fund) and 277 positions, an increase of \$553,000 and 2 positions.

**Context for Staffing Discussion:** The Department's budget was discussed at the March 14 hearing and the Subcommittee left all budget issues open for further review of the sufficiency of the staffing request. A January 2007 State Auditor Report indicated that, among other findings, the Department has not, contrary to law, conducted at least 170 (37 percent) of its required examinations of escrow office licensees within the last four years. In addition, it has yet to conduct examinations for 899 (35 percent) of eligible finance lender licensees within its four-year goal. The Department testified that the Governor's Budget did not include sufficient new positions to allow the department to meet all audit requirements, but that the 2008-09 Governor's Budget would include further adjustments. The Subcommittee was concerned about the Department being unable to meet statutory audit requirements and the associated financial risk that places on consumers. The Administration agreed to reevaluate 2007-08 staffing and has submitted two May Revision Finance Letters that would add another 25 positions to the Department's budget. In discussions with Committee staff, the Department indicated that up to 112 new positions might be needed over the long term to fully address all audit issues – the Department of Finance indicates that it will continue to work with the department to produce a comprehensive staffing analysis and plan, and the 2008-09 Governor's Budget will include additional adjustments as warranted. *(Note, for brevity the net increase of 2 positions in the January Governor's Budget via BCP #1 [extension of 3 limited-term positions & \$342,000] and BCP #2 [addition of 2 new positions & \$159,000] are not included in the issues below –those are included in the Governor's Budget and can be approved without a vote).*

**Context for Funding Discussion:** Statute requires Corporations to reduce its fund balance to maintain a fund balance not to exceed 25 percent of annual expenditures. The Governor's Budget indicates the State Corporation Fund would end 2006-07 with a reserve of \$9.0 million. Additionally, there is a loan outstanding to the General Fund of \$18 million.

**Issues for Discussion / Vote**

- 1. Lender-Fiduciary Program: Staffing Augmentation (May Finance Letter #1).** The Administration requests \$2.3 million (special fund) and 18.0 new Examiner positions in the Lender-Fiduciary Program which would be allocated to the following sub-programs: 3.0 positions for the California Deferred Deposit Transaction Law (CDDTL) – which includes “pay-day lenders;” 11.0 positions for Escrow Law (Escrow); and 4.0 positions for the California Residential Mortgage Lending Act (CRMLA). The Examiner positions will help address the substantial increase in workload associated with statutorily-mandated examinations, provide an adequate level of industry regulation, and help ensure consumer protection against lending and financing fraud. While these new positions represent a large improvement from the number included in the Governor’s Budget, the Administration indicates that more positions will likely be needed in future budgets to fully meet all statutory audit requirements.

**Staff Comment:** At the past hearing, the Subcommittee had expressed particular concern about the payday lending industry, which is part of the CDDTL program (3.0 new positions are requested). The payday lending industry has only been licensed and audited by the department since 2004-05, and the number of licensees has grown by 30 percent since then. Statute requires that Corporations audit each payday lending business not less than once every two years. Discussions with the department suggest that addition Examiners (beyond this May Finance Letter) will be needed to meet all statutorily-required audits. While the Department might not realistically be able to address all staffing deficiencies in a single year, the Subcommittee may want to consider fully staffing the audit function for the payday-lending industry. Staff believes an augmentation of 5.0 positions (and related funding) should allow the department to staff to a level that would provide the consumer protections outlined in statute.

**Staff Recommendation:** Approve the May Finance Letter, but add an additional 5.0 Examiners and \$648,000 (special fund) to fully meet statutory audit requirements for the payday lending industry.

- 2. Enforcement: Staffing Augmentation (May Finance Letter #2).** The Administration requests \$973,000 (special fund) and 7.0 additional positions (1.0 Examiner and 6.0 Counsels) to improve the Department’s response time to complaints from the public and to effectively pursue those who commit predatory investment, lending and financial fraud against consumers. The Department indicates that since staffing was reduced by 40 percent in 2002-03 and 2003-04, Corporations has had to reject cases because of insufficient staff resources. The Department estimates it will have to annually reject 72 cases without investigation if current staffing is not increased. The new positions would assist in processing new complaints and prevent a potential backlog of complaints and cases. The result of obtaining the additional positions will be quicker investigations and increased chances of obtaining restitution for victims of financial crime.

**Staff Comment:** As an additional measure of staffing need, the Department compared enforcement staffing to similar departments in other large states. California is proportionally understaffed relative to the other states studies – for example both Texas



and California have current enforcement staff of 36 positions, but California has 283,000 licensees versus 180,000 in Texas.

As was suggested in the last issue, the staffing augmentation may not be sufficient, and additional staffing increases may be warranted in the 2008-09 budget. So the Legislature can stay informed on Corporations enforcement activities, Staff recommends the Subcommittee adopt Supplemental Report Language.

**Supplemental Report Language:** *The Department shall report to the appropriate fiscal and policy committees of the Legislation no later than September 1, 2007, and March 1, 2008, and every September 1 and March 1 thereafter through March 1 2011, on the Department's enforcement efforts. The report shall include, but need not be limited to, the following data from the prior six-months of enforcement activity:*

- 1) The number of authorized enforcement positions and the number of vacancies.*
- 2) The total number of complaints received; the number of complaints that were resolved without opening a case; the number of complaints that resulted in cases being opened and the number of cases opened that resulted in an enforcement action.*
- 3) The number of complaints and cases, if any, that were rejected due to insufficient staff resources.*
- 4) The average time to close an enforcement case.*
- 5) The amount of consumer restitution resulting from enforcement actions and the amount of penalty or fine revenue received by the Department from enforcement actions.*
- 6) The following data on specific programs as defined by California Financial Code Section:*
  - a) Section 23058: The number of citations issued by the department, a description of what the citations issued for, and a description of the violations.*
  - b) Section 23052: The number of licenses revoked or suspended and a description of the reasons for the revocation or suspension.*
  - c) Section 23051: The number of civil actions the department brought to enforce the California Deferred Deposit Transaction Law and a description of the basis of the actions.*
  - d) Section 23060: The number of contracts the department voided because a consumer was overcharged.*
  - e) Section 23050: The number of cease and desist orders the department issued against: (1) unlicensed operators or (2) licensed operators and a description of the violations at issue.*
- 7) An update on how the department's efforts to "migrate" some of their enforcement techniques into the examination process is working, including the number of citations issued per this new policy, and a description of what violation for which the licensee was cited.*
- 8) Each subsequent report shall include numerical data from the prior reports for comparison purposes.*

**Staff Recommendation:** Approve the May Finance Letter, but also adopt the suggested "placeholder" Supplemental Report Language.

## **2240 Department of Housing and Community Development**

A primary objective of the Department of Housing and Community Development (HCD) is to expand housing opportunities for all Californians. The Department administers housing finance, economic development, and rehabilitation programs with emphasis on meeting the shelter needs of low-income persons and families, and other special needs groups. It also administers and implements building codes, manages mobilehome registration and titling, and enforces construction standards for mobilehomes.

The Governor proposes \$968.6 million (\$15.6 million General Fund) and 597.2 positions for the department – an increase of \$314.3 million (48 percent) and 70.3 positions.

The majority of the Department's expenditures are supported by general obligation bond revenue. The budget includes \$58 million from the Emergency Shelter Trust Fund Act of 2002 (Prop 46) – down by \$170.8 million from 2006-07 due to the full expenditure of bond funds for some programs. The budget includes \$659.4 million from the Housing and Emergency Shelter Trust Fund Act of 2006 (Prop 1C). Portions of Prop 1C funds are continuously appropriated, and the Department is using this existing authority to expend \$161 million in Prop 1C funds in 2006-07.

The second largest revenue source is federal funds, estimated at \$174.5 million in 2007-08, which is about the same as 2006-07. Remaining expenditures of about \$77 million are covered by the General Fund (\$15.6 million), fees, and other miscellaneous revenues.

### **Issues proposed for Consent / Vote-Only**

- 1. Community Development Block Grant (CDBG) Staffing (BCP#8).** The Administration requests \$444,000 (federal funds) and 4.0 positions to better meet federal requirements for program monitoring and reporting. The primary objective of the CDBG program is that development of viable rural and small urban communities by providing decent housing and a suitable living environment, funding public works including infrastructure and by expanding economic opportunities, principally for lower income households. HCD indicates that the four additional positions would also increase the timeliness of disbursement to localities of the federal funds. This budget request was inadvertently left off the March 14, 2007, Subcommittee agenda – so this is the first time this issue is before the Subcommittee.

**Staff Recommendation:** Approve the issues on the consent / vote-only list.

**Vote:**

**Issues for Discussion / Vote:**

- 1. Housing and Emergency Shelter Trust Fund Act of 2006 (Prop 1C).** Prop 1C provides for a general obligation bond issuance not to exceed \$2.85 billion. The Governor proposes to expend \$653.0 million of Prop 1C revenues in 2007-08 (excluding \$6.4 million and 45 new positions for administration). Using existing expenditure authority, the Department plans to spend \$160 million in 2006-07 (excluding \$1 million for administrative costs), for a combined two year total of \$820 million. Some Prop 1C programs are already continuously appropriated and other programs require a Budget Act appropriation to authorize expenditure. The Administration has submitted budget trailer bill language to fully implement the Prop 1C programs. The chart below outlines proposed Prop 1C expenditures by category and indicates whether each program will be administered by the Housing and Community Development (HCD) Department, or by the California Housing Finance Authority. Dollars are in thousands and 2006-07 and 2007-08 allocations exclude administrative costs.

<b>Proposition 1C Category</b>	<b>2006-07 Allocations</b>	<b>2007-08 Allocations</b>	<b>Total Prop 1C</b>	<b>Approp Type</b>	<b>Budget</b>
<b><u>Homeownership Programs</u></b>					
CalHome	\$35,000	\$55,000	\$290,000	Continuous	HCD
CA Homeownership Program (BEGIN)	0	40,000	125,000	Budget Act	HCD
Self-Help Housing Program	0	3,000	10,000	Continuous	HCD
CA Homebuyers Down-payment Assistance Program	0	15,000	100,000	Continuous	CalHFA
Residential Development Loan Program	0	15,000	100,000	Continuous	CalHFA
Affordable Housing Innovation Fund	0	15,000	100,000	Budget Act	HCD
<b><u>Multifamily Rental Housing Program</u></b>					
General	70,000	140,000	345,000	Continuous	HCD
Supportive Housing	20,000	80,000	195,000	Continuous	HCD
Homeless Youths	15,000	15,000	50,000	Continuous	HCD
<b><u>Other Programs</u></b>					
Serna Farmworker Loans/Grants	20,000	40,000	135,000	Continuous	HCD
Emergency Housing Assistance	0	10,000	50,000	Continuous	HCD
Infill Incentive Grants	0	100,000	850,000	Budget Act	HCD
Transit Oriented Development	0	95,000	300,000	Budget Act	HCD
Housing Urban-Suburban and Rural Parks	0	30,000	200,000	Budget Act	HCD
<b>TOTAL</b>	<b>\$160,000</b>	<b>\$653,000</b>	<b>\$2,850,000</b>		

**Staff Comment:** Generally, the Administration proposes to expend Prop 1C funds over a 3-to-5 year period depending on the program. For programs with a budget bill appropriation, HCD is requesting appropriations to cover only 2007-08 expenditures (the Department of Transportation is requesting appropriations to cover anticipated expenditures over a three-year period).

The Subcommittee may want to consider the following when taking action on the Prop 1C budget proposal:

- Several Senate bills are under consideration to implement Prop 1C programs, among these are SB 46 – Perata; SB 522 – Dutton; and SB 546 – Ducheny. These bills provide alternative implementing language to that included in the Administration’s trailer bills.
- The Incentive Infill Grant Program is an \$850 million dollar program, but only \$100 million is proposed for appropriation in 2007-08, the Subcommittee may want to consider increasing that amount.
- The Housing Urban-Suburban and Rural Parks program could alternatively be placed in the Department of Parks and Recreation, since they have prior experience with administering grants for parks. Since the bond language specifies “housing-related parks grants,” the Legislature may want retain a prominent role for HCD (in a coordination and advisory role) if the program is moved to the Department of Parks and Recreation.

**Staff Recommendation:** Staff recommends the following actions:

- Reject the Administration’s Prop 1C trailer bill language and adopt placeholder trailer bill language. This action would put the trailer bill language into the Conference Committee.
- Increase the budget bill appropriation for the Incentive Infill Grant Program from \$100 million to \$300 million.
- Delete the \$30 million appropriation in the HCD budget for the Housing Urban-Suburban and Rural Parks program.

- 2. Proposition 1C Staffing and Associated Administrative Costs (BCP #3).** The Administration requests \$6.4 million (various funds) and 45.0 new positions to perform workload associated with Proposition 1C. The request includes out-year budget adjustments for annual changes in workload (the 2008-09 request is for \$10.5 million and 71.0 positions). HCD data suggest the overall administrative cost over the life of Prop 1C programs will average about 4.8 percent, which is under the 5.0 percent level deemed acceptable.

**Staff Recommendation:** Adjust staffing to conform to the action taken on Issue #1. If the Subcommittee adopts the Staff Recommendation for Issue #1, the Incentive Infill Grant Program staff should be augmented and the Suburban and Rural Parks program staff should be reduced. Since the implementing trailer bill language will be in Conference Committee, further adjustments to HCD staffing can be made in Conference, as warranted.

## 2660 Department of Transportation

### Issues Proposed for Vote Only:

- 1. Transfer of Fleet Management for Cars and Light Trucks to DGS (May Revision Finance Letter):** The Administration requests \$912,000 (State Highway Account) to pay the Caltrans share of Department of General Services' (DGS) redistributed fleet management fees. DGS re-issued its *State of California Fleet Handbook* on January 2, 2007, which specifies that under Government Code Section 11000, all State agencies owning or leasing vehicles or other mobile equipment are subject to DGS oversight under the auspices of the State Fleet Asset Management Program. The May Finance letter would provide Caltrans a budget augmentation to pay this new DGS assessment. Staff recommends approval of this May Letter
- 2. Technical Corrections to the Governor's Budget (May Revision Finance Letter):** The Administration requests adjustments to the budget bill to correct the scheduling of expenditures by budget item. Also included in the request is a shift of federal funds and State Highway Account funds to accommodate revised federal guidance on eligible expenditures. None of these adjustments change net expenditures, nor is net federal funding reduced. Staff recommends approval of this May Letter.
- 3. Prop 42 – Minor Forecast Adjustments (May Revision Finance Letter):** The Administration requests a decrease of \$8.6 million in 2006-07 (to \$1.419 billion) and an increase of \$5.4 million in 2007-08 (to \$1.481 billion) in Proposition 42 gasoline sales tax revenue and proposes various adjustments to update the budget to reflect the new revenue estimates. Staff recommends approval of this May Letter.
- 4. Prop 42 Loan Repayments (Governor's Budget Trailer Bill):** The Administration requests trailer bill language to amend statute to conform to the Proposition 42 loan repayment requirements of Proposition 1A, approved by voters in November 2006. Prop 1A amended Article XIXB of the California Constitution to require full repayment of Proposition 42 loans made in 2003-04 and 2004-05 to the General Fund by June 30, 2016. Article XIXB requires yearly repayments at a minimum of one-tenth of the amount outstanding on July 1, 2007. Staff recommends approval of the trailer bill language, including any technical amendments that might be warranted.

**Staff Recommendation:** Approve the staff recommendations for all the vote only issues listed above.

**Issues for Discussion and Vote:**

- 5. Proposition 1B – Appropriations and Statutory Implementation (May Revision and Trailer Bill Language).** The Highway Safety, Traffic Reduction, Air Quality, and Port Security Bond Act of 2006 (Prop 1B) provides for a general obligation bond issue not to exceed \$19.925 billion. The May Revision of the Governor's Budget requests appropriations totaling \$11.487 billion in Prop 1B bond funds, although only \$4.087 billion is expected to be allocated, or committed, in 2007-08. Dollars below are in thousands.

<b>Proposition Category</b>	<b>1B</b>	<b>2007-08 Allocations</b>	<b>2008-09 Allocations</b>	<b>2009-10 Allocations</b>	<b>2007-08 Appropriations</b>	<b>Total 1B Amount</b>	<b>Budget</b>
Corridor Mobility Improvement Account (CMIA)		\$610,000	\$1,577,000	\$1,229,000	\$3,416,000	\$4,500,000	Caltrans
Transit		600,000	350,000	350,000	1,300,000	3,600,000	State Trans Assistance
State Transportation Improvement Program (STIP)		739,000	799,000	274,000	1,812,000	2,000,000	Caltrans
Local Streets & Roads		600,000	300,000	150,000	1,050,000	2,000,000	Shared Revenues
Trade Infrastructure		202,000	302,000	302,000	806,000	2,000,000	Caltrans
State Highway Operations and Preservation Program (SHOPP)		405,000	267,000	24,000	696,000	750,000	Caltrans
State/Local Partnership		202,000	197,000	200,000	599,000	1,000,000	Caltrans
Grade Separations		123,000	123,000	0	246,000	250,000	Caltrans
State Route 99 Improvements		16,000	109,000	302,000	427,000	1,000,000	Caltrans
School Bus Retrofit*		97,000	97,000	0	194,000	200,000	Air Resources Board
Local Bridge Seismic Retrofit		14,000	11,000	11,000	36,000	125,000	Caltrans
Trade Infrastructure Air Quality*		111,000	0	0	111,000	1,000,000	Air Resources Board
Port / Transit Security**		178,000	123,000	101,000	402,000	1,100,000	Office of Emerg Svc
Intercity Rail		190,000	74,000	128,000	392,000	400,000	Caltrans
<b>TOTAL</b>		<b>\$4,087,000</b>	<b>\$4,329,000</b>	<b>\$3,071,000</b>	<b>\$11,487,000</b>	<b>\$19,925,000</b>	

\* These Prop 1B Appropriations will be heard in Subcommittee #2

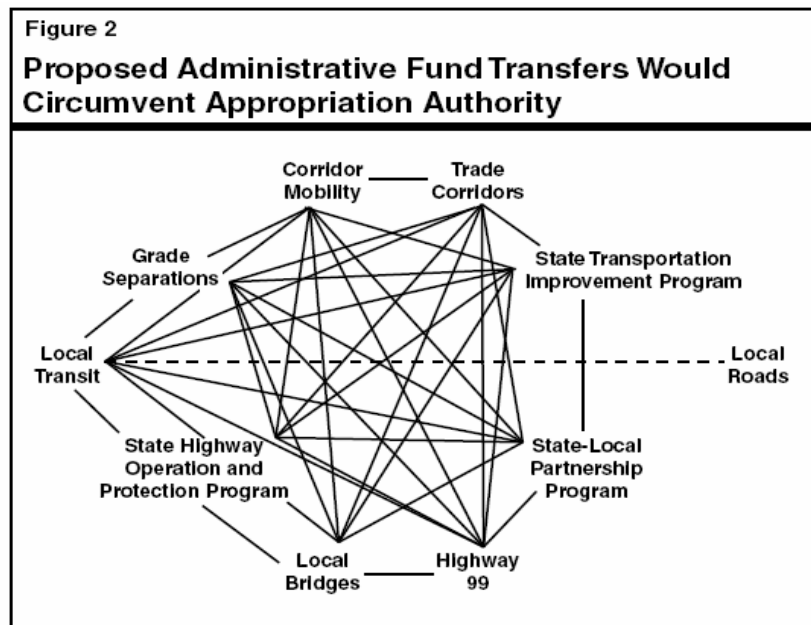
\*\* This Prop 1B Appropriation was considered by the Subcommittee when the Office of Emergency Services was heard.

While many past bond revenues have been continuously appropriated upon bond passage, Prop 1B funds require an appropriation by the Legislature to expend the funds. The Administration is requesting an appropriation level that will cover

anticipated expenditures through 2009-10. This means that the Administration would not have to come forward with a Prop 1B appropriation request in either the 2008-09 or 2009-10 budgets.

The Administration has submitted statutory changes to implement certain Prop 1B programs. Several Senate bills are also under consideration to implement Prop 1C programs, among these are SB 286 – Lowenthal & Dutton; SB 9 – Lowenthal; SB 748 – Corbett; SB 716 & SB 45 – Perata; and SB 784 – Torlakson. These bills provide alternative implementing language to that included in the Administration's trailer bill.

**LAO Recommendations:** In the *Analyses of the 2007-08 Budget Bill*, the Legislative Analyst recommends that the Legislature maintain oversight for bond programs by appropriating funds annually (as opposed to the three-year appropriation proposed). Finally, the LAO recommends deletion of budget bill language that would allow the Administration to shift appropriation authority among bond programs. Figure 2 from the *LAO Analysis* is copied below to illustrate the requested transfer flexibility.



**Staff Recommendation:** Staff recommends the following actions:

- Reject the Administration's Prop 1B trailer bill language and adopt placeholder trailer bill language. This action would put the trailer bill language into Conference Committee.
- Reject the multi-year appropriations and appropriate only the amount identified in the May Revision for allocation in 2007-08 and delete related budget bill language.

- Adopt new budget bill language for the following bond categories that would allow the Director of Finance to augment the 2007-08 appropriations by up to 25 percent of the 2008-09 estimated appropriation need (to accommodate any projects that may be ready for allocations sooner than currently anticipated – the actual dollar estimates should be included in the budget language): CMIA, STIP, SHOPP, Route 99, Local Bridge Seismic (see above table for key to acronyms).
- Reduce the Local Streets and Roads appropriation to \$400 million. The Administration proposes \$600 million in 2007-08, \$300 million for 2008-09 and \$150 million for 2009-10. Spreading the funding more evenly across the years may allow more effective state oversight, whether that oversight is provided by the Controller or the California Transportation Commission, by reducing the number of projects for review in 2007-08 while appropriate review structures are developed. Additionally, spreading the funding more evenly across years may reduce project costs by reducing the project bubble for contractors who do local street and road work.
- Reject budget bill language that would allow the Administration to shift appropriation authority among bond programs.
- Amend budget bill language to provide the standard 3 years to allocate bond projects instead of the 4 year period requested in the January budget bill.
- Action on this issue should include the conforming action in the 2640 budget item (State Transit Assistance) where the Transit Prop 1B funding is appropriated and in the 9350 budget item (Shared Revenue) where the Local Streets and Roads Prop 1B funding is appropriated. Additionally, Provision 1 of the 9350 item specifies allocation by the California Transportation Commission, but SB 286 (Lowenthal and Dutton) specifies allocation by the State Controller – therefore, delete this provision. (This language can be further amended in Conference, as required, to conform to the final package).



- 6. Proposition 1B – Administrative Staffing (May Finance Letter):** The Administration requests \$13.4 million (Prop 1B bond funds) and 112.0 new three-year limited-term positions to provide administrative staffing for Prop 1B workload in the non-Capital-Outlay-Support (COS) areas. The request for COS workload, which includes engineering, review, and oversight of capital outlay projects, is requested in a separate May Finance Letter that is discussed in the following issue.

**Background / Detail:** The request includes the following elements:

- \$5.3 million and 49.0 positions in the Local Assistance Program for workload associated with CMIA, STIP, State-Local Partnership, and Traffic Light Synchronization. (See the table included in the prior issue for a description of the acronyms.)
- \$1.1 million and 6.0 positions for Program Development for workload associated with Local Bridge Seismic Retrofit.
- \$3.7 million and 19.0 positions for the Mass Transportation Program for workload associated with transit, intercity rail and grade separation.
- \$122,000 and 1.0 position for Transportation Planning to develop and implement Trade Corridors Improvement projects.
- \$4.6 million and 37.0 positions for the Division of Accounting (31 positions), the Division of Budgets (5.0 positions) and the Division of Audits (1 position)

**LAO Recommendation.** The Legislative Analyst recommends a total reduction of \$3.67 million and 42.4 Personnel Years (PYs) in 2007-08. (the dollar value associated with the reductions are estimates; and may need modification after further discussions with the Administration). Discussions with the Administration indicate that this request may overstate actual workload needs in 2007-08. In general, workload estimates assume that Proposition 1B programs, such as State-Local Partnership (SLP), would fund project development beginning July 1, 2007, and that Caltrans would have a role in administering Local Transit, as well as Local Streets and Roads program funds. It is likely that the Legislature would want to revisit Caltrans' personnel resource requirements in 2008-09, when workload can be better assessed. The LAO recommends the following specific reductions:

- **Accounting.** Reduce by 10 PYs and about \$700,000. It is unclear, at this time, whether the division will need the PYs requested to address accounting workload related to the Local Transit, Local Streets and Roads, and SLP programs. This is because the Legislature has not decided whether Caltrans will be involved in administering funds for the Local Transit and Local Streets and Roads programs. Moreover, it is unclear how much accounting workload would be generated by the SLP program in 2007-08, as projects are unlikely to be selected before early 2008.
- **Local Assistance.** Reduce by 22 PYs and about \$2 million. A large part of the estimated workload is related to implementation of the SLP program. Discussions with the administration suggest that the workload estimate assumes that 415 SLP projects are selected by July 1, 2007 and generate immediate workload by Local Assistance. Because it is highly unlikely that these projects

would be selected before early 2008, we recommend reducing the administration's request.

- **Mass Transportation.** Reduce by 5.5 PYs and about \$450,000. The administration's request for 9.5 PYs is not justified by the expected increase in workload in 2007-08. Discussions with the department indicate that the increase in workload will only likely occur if total funding to transit projects increases. Reductions in PTA revenues to transit programs as proposed in the Governor's budget will offset much of the additional workload resulting from the \$600 billion in Prop 1B funds being appropriated to this program. In the past, the department has absorbed changes in workload without increasing PYs, even when funding levels have fluctuated significantly.
- **Rail - Grade Separation.** Accept request for 3 PYs but reject \$12,000 request for out-of-state travel. The influx of Prop 1B funds in 2007-08 will increase funding for this program significantly. While it is still unclear how greatly workload will increase, the request for PYs seems reasonable. The request for \$12K for out of state travel is not justified and we recommend deleting this amount.
- **Rail - Procurement.** Reduce by 4 PYs and about \$500,000. A large part of the estimated workload would not be able to begin until after the completion of an audit of the existing rail fleet and an analysis of ridership and revenue projections. Discussions with the administration indicate that the audit will not be complete until about February 2008. Furthermore, the results of the audit and projections could impact the number and specifications of the railcars and locomotives to be purchased. Since it is unlikely that the much of the increased workload will occur prior to February 2008, we recommend reducing the administration's request.
- **Planning.** Delete the requested .9 PY and \$8,000. Due to the small size of the request we recommend the department absorb any increase in workload with existing staff.

**Staff Comment:** The LAO's recommendations provide the Subcommittee a reasonable set of actions relative to the information known at this time. Some of the workload associated with Prop 1B is dependent on how the Legislature chooses to implement certain Prop 1B programs. Overall Proposition 1B implementation will be discussed further in the Conference Committee. After the Legislature determines what statutory changes are appropriate to implement Prop 1B programs, further budget changes may be warranted for administrative staffing.

**Staff Recommendation:** Adopt the LAO recommendation – reduce the Administration's request for \$13.4 million and 112.0 new positions, by \$3.67 million and 42.4 personnel years.

- 7. Capital Outlay Support (COS) (May Finance Letter).** The Administration requests an augmentation of \$206 million (various funds including Prop 1B bond funds), a reduction of 100 state staff positions, and an increase of 595 contract-out resources. This request would result in total COS resources of \$1.8 billion and 13,121 full-time equivalents (FTEs) composed of 10,515 state staff, 668 FTEs of state-staff overtime, and 1,938 FTEs of contracted staff resources. Included in the request is funding of \$63.2 million to fully fund the cost of existing state staff – Caltrans indicates it is underfunded for position costs, and has been forced to maintain higher vacancies at the beginning of each year to produce savings. The request indicates that 640 FTEs are associated with Prop 1B COS workload, along with about \$119 million in Prop 1B funds.

**Background / Detail:** Every year, there is significant discussion between the Administration and Legislature concerning the appropriate split of COS workload between state staff and contract resources. There is also debate over the relative cost of state staff versus contract resources. The numbers assumed by the administration in compiling the budget request are that state staff cost \$126,000 (including all benefits and the standard cost of operating expenses and equipment) and contract out resources cost \$209,000 per FTE. However, Caltrans argues that additional overhead are associated with state staff that might appropriately increase the cost of state staff to \$150,000 for comparison purposes. For budgeting purposes, staff recommends the Subcommittee consider the cost of state staff at \$126,000 and contract resources at \$209,000 per full time equivalent – the number used by the Administration in the budget request. For comparison purposes, the following “Full Time Equivalent” chart was developed, with assistance from Caltrans.

Year	State Staff	Overtime	Contract Out	Total
1988-89	6,796.2	292.0	1,047.0	8,135.2
1989-90	7,072.3	310.0	937.0	8,319.3
1990-91	7,901.5	352.9	1,207.0	9,461.4
1991-92	8,789.2	379.4	1,305.0	10,473.6
1992-93	8,760.6	379.4	1,285.0	10,425.0
1993-94	8,696.0	305.0	855.0	9,856.0
1994-95	8,394.0	299.0	801.0	9,494.0
1995-96	7,782.0	298.0	803.0	8,883.0
1996-97	7,164.0	298.0	1,306.0	8,768.0
1997-98	7,538.0	351.0	1,176.0	9,065.0
1998-99	9,434.2	691.5	921.0	11,046.7
1999-00	9,854.3	546.0	592.0	10,992.3
2000-01	10,565.3	821.9	1,159.0	12,546.2
2001-02	11,072.0	650.0	1,646.0	13,368.0
2002-03	10,803.0	650.0	1,382.0	12,835.0
2003-04	10,245.0	303.0	500.0	11,048.0
2004-05	10,651.0	699.0	1,070.0	12,420.0
2005-06*	11,200.0	710.0	1,568.0	13,478.0
2006-07*	10,638.0	636.0	1,410.0	12,684.0
2007-08 Proposed	10,515.0	668.0	1,938.0	13,121.0
<b>Long-run average %</b>	<b>85%</b>	<b>4%</b>	<b>10%</b>	
<b>2006-07 (at Budget Act)</b>	<b>84%</b>	<b>5%</b>	<b>11%</b>	
<b>2007-08 (Proposed)</b>	<b>80%</b>	<b>5%</b>	<b>15%</b>	

\* At the time of the Budget Act - excludes mid-year adjustments

**LAO Recommendation:** The Legislative Analyst believes that the total level of personnel resources requested by the department is reasonable, and appropriate mix of state staff versus contracted resources is a policy decision for the Legislature. The LAO offers another option for budgeting Prop 1B bond funds:

Option for Budgeting State Operations Funds. Currently, the administration proposes to fund state operations activities related to Proposition 1B implementation through individual appropriations by each Proposition 1B account. These state operations activities include the COS resources requested in this issue, as well as the administrative resources requested in issue 201. Discussions with the administration indicate that it is very difficult to estimate the exact level of funding that should be appropriated from each account to state operations activities related to Proposition 1B. This is because some programs have yet to be fully developed and thus, the exact amount of state resources required to administer programs and provide capital outlay support are unknown. To address this uncertainty, the administration request flexibility to transfer state operations appropriations between programs. (While this provides the needed flexibility, it also creates additional workload for the department to track movement of expenditure authority among Prop 1B accounts. Over time, this workload can become unwieldy and very cumbersome.)

Recognizing this uncertainty, we are offering an alternative approach for budgeting state operations expenditures of Proposition 1B funds. The Legislature may want to consider creating a separate, consolidated Proposition 1B account designated for state operations expenditures. Under this option, the budget would transfer a specified percentage of funds from each Proposition 1B account into the new consolidated state operations account rather than making separate appropriations for state operations items from each Proposition 1B account.

Some advantages to this approach include:

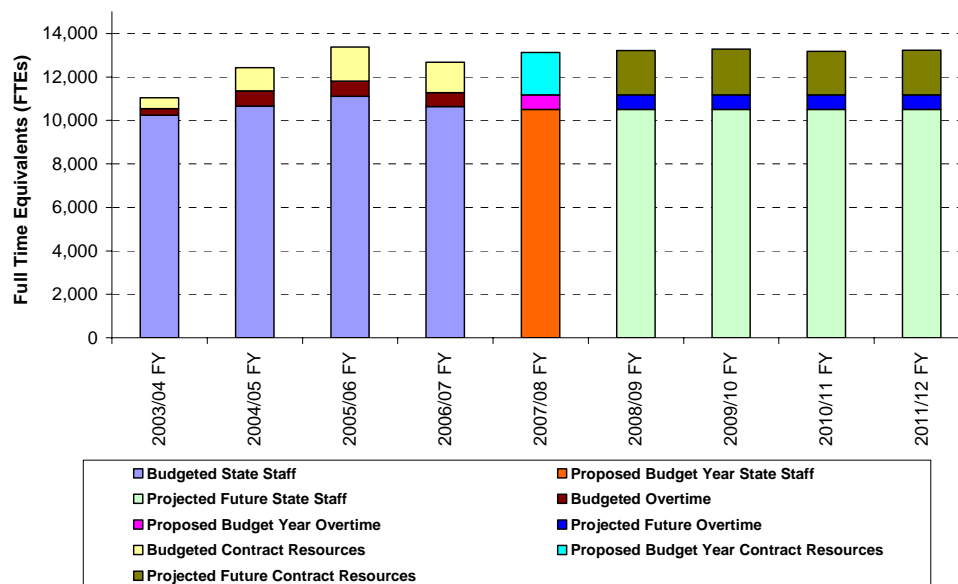
- (1) Cleaning up budget bill language by simplifying state operations appropriations and deleting flexibility provisions;
- (2) Saving time for the administration in tracking state operations activities (it would be much simpler to estimate total Proposition 1B state operations expenditures than to track what percentage of hours is attributable to a specific account);
- (3) Increasing accountability by limiting the total percentage of Proposition 1B funds spent on state operations to a percentage that the Legislature finds acceptable.

**Staff Comment:** By whatever measure is chosen, state staff are less expensive than contract-out staff. However, it is beneficial to maintain a certain level of contractor work to even out the peaks and valleys in workload across the state and in individual districts, and to prevent the need for layoffs when the workload drop is dramatic. Additionally contract staff may be desirable where unique experience is

needed for a specific project. As the table indicates, the Administration is requesting a higher-than-average level of contract staff and a lower-than-average level of state staff. Given the \$83,000 cost difference between state staff and contract staff (based on how Caltrans budgets the costs), adjusting the budget back to the long-run average of 90 percent state resources and 10 percent contract resources (by shifting 595 contract FTEs back to state staff) would result in a savings of about \$50 million.

Shifting 595 contract resources to state staff (a net increase of 467 state staff relative to the 2006 Budget Act level) would seem feasible from the perspective of recruiting (relative to past staffing increases as displayed on the table). While bond workload may represent a bit of a workload boom, the *draft* long-term workload estimates provided by Caltrans do not suggest a dramatic drop in overall workload anytime in the next five years (state staff is the bottom bar, state staff overtime is the middle bar, and contract work is the top bar).

Chart 3 - Historic, Budget Year and Projected Future Capital Outlay Support Resources



The LAO recommendation on setting up a new account for Prop 1B state operations expenses merits additional discussion. Since Prop 1B issues will be further discussed in Conference, staff recommends no action on that LAO proposal at this time.

**Staff Recommendation.** Shift 595 contract resources to state staff to achieve a savings of approximately \$50 million. Direct staff to work with the Administration to primarily shift workload funded by the State Highway Account (SHA) and federal funds (instead of Prop 1B funds or other funds) – this will produce SHA savings that could be used for needed maintenance or State Highway Operation Protection Program (SHOPP) projects.

**8. Shift Public Transportation Account Revenues to Pay General Fund Obligations (Governor's Budget).** The Governor's January Budget proposed to shift \$1.1 billion in Public Transportation Account (PTA) funds to pay the following State obligations, which are currently the responsibility of the General Fund:

- \$627 million for Home-to-School Transportation (currently Proposition 98).
- \$340 million for transportation-related general obligation bond debt.
- \$144 million for regional center transportation budgeted in the Department of Developmental Services.

Based on a revised revenue forecast, a May Revision Finance Letter proposed to increase the amount of this shift to \$1.3 billion, with an additional shift of \$200 million to Home-to-School Transportation.

**Background / Detail:** The PTA will receive an estimated \$827 million in "spillover" funds in 2007-08 – up from the revised estimate of \$551 million for 2006-07. The proposed shift would exceed the 2007-08 amount of the volatile spillover revenues, which have materialized in recent years due to high gasoline prices, and also expend non-spillover PTA revenues. The Administration indicates this shift will not have a major impact, in the short-term, on transit capital projects because of bond and other funding resources. The California Transportation Commission (CTC) indicates that some portion of the \$568 million in mass transit projects programmed for 2007-08 allocations in the State Transportation Improvement Program (STIP), will have to be shifted to Prop 1B bond funds, or other STIP funding sources that would otherwise be available for highway projects. The proposal would represent a major reduction in what local transit agencies would otherwise receive for operations in 2007-08 (current statute directs half of the spillover, or about \$414 million to local transit agencies – see also the State Transit Assistance budget later in this agenda).

The Administration proposes to permanently redirect spillover funds to pay current General Fund obligations. If this proposal were approved and spillover revenue averages about \$600 million each year, the total loss to mass transportation over the next five years would total around \$3.5 billion (which is similar to the amount included in Proposition 1B for mass transit).

**LAO Recommendation:** In the Education Section of the *Analysis of the 2007-08 Budget Bill*, the Legislative Analyst indicated the Administration's January plan for Home-to-Schools portion of this proposal involved the "re-benching" of Proposition 98, which was likely unconstitutional. An April Finance Letter revised the Home-to-Schools proposal such that the PTA funding reimbursed the General Fund cost and Prop 98 would not be rebenching – the LAO indicates that the revised Home-to-Schools proposal is also legally unworkable.

**Staff Recommendation:** Reject this proposal, including related trailer bill language. While this proposal might be further discussed in the Budget Conference Committee or final budget negotiations, the proposal raises many concerns that remain unaddressed at this time.

- 9. Non-Article XIX Funding (Trailer Bill Language).** The Administration proposes to amend statute to permanently retain approximately \$65 million in annual miscellaneous revenues, which are not subject to the expenditure restrictions in Article XIX of the Constitution, in the State Highway Account (SHA) instead of transferring these revenues to the Public Transportation Account (as specified by Section 183.1 of the Streets and Highways Code).

**Background / Detail:** This miscellaneous revenue is primarily derived from the rental and sale of Caltrans property originally purchased for highway purposes. Because the revenue is not restricted by Article XIX, it can be expended for either highway or mass transportation purposes. Prior to 2000-01, and the addition of Section 183.1, the funding was retained in the SHA. Since 2000-01, the funding has been transferred to the PTA, except in 2003-04 and 2004-05 when the funding was retained in the SHA by budget bill language.

**Staff Comment:** If the Subcommittee accepted the Staff Recommendation on the prior issue and rejected the shift of \$1.3 billion in PTA funds to support General Fund obligations, the Administration proposal to retain non-Article XIX in the SHA for 2007-08 would appear warranted. The SHA funds maintenance and SHOPP activities that are constrained due to SHA cash balances. However, staff recommends the Subcommittee consider this shift on a one-time basis and not delete Section 183.1 of the Streets and Highways Code.

**Staff Recommendation:** Reject the Administration's trailer bill language to repeal Section 183.1 of the Streets and Highways Code, which directs the annual transfer of non-Article XIX revenues from the SHA to the PTA. Adopt budget bill language to allow non-Article XIX funds to be retained in the SHA in 2007-08 (only), notwithstanding Section 183.1.

**10. Allocation of Tribal Gaming Revenue (Governor's Budget and April Finance Letter):** The January Budget Bill included new budget bill language to track expenditure of tribal gaming money that is received from five tribes pursuant to gaming compacts ratified in 2004. The State is receiving about \$100 million annually from these tribes for transportation. The revenue stream was originally intended to support bonds, but litigation has delayed the issuance of bonds and the revenue stream is available for transportation expenditures pending resolution of legal issues for the bond issuance. The revenue supports the repayment of transportation loans made to the General Fund prior to 2003-04. The April Finance letter made modifications to the proposed budget bill language as follows:

***Budget Bill Language*** - *Provision 5 of Item 2660-302-0042. The funds appropriated in this item include \$100 million attributable to the tribal gaming revenue collected and deposited in the State Highway Account pursuant to Section 63048.65 of the Government Code. These funds shall only be available for pavement rehabilitation projects programmed in the State Highway Operation and Protection Program (SHOPP), and shall not supplant any other funding available for SHOPP. The first \$100 million of the SHOPP projects allocated using the appropriation provided by this item shall be funded from tribal gaming revenue deposited into the State Highway Account. The Department shall monitor the allocation and expenditure of these funds and report on their status upon request of the Department of Finance.*

**Staff Comment:** The tribal revenue is available to repay loans to both the Public Transportation Account (PTA) and State Highway Account (SHA), although existing statute directs that the SHA be repaid first. If the Subcommittee accepted the staff recommendation on the earlier issue and rejected the shift of \$1.3 billion in PTA funds to support General Fund obligations, the Administration proposal to direct the tribal revenue to the SHA (instead of the PTA) seems warranted. The SHA funds highway maintenance and SHOPP activities that are constrained due to SHA cash balances. No concerns have been raised with the revised budget bill language. Staff understands the tribes are supportive of the language because they would like to know what transportation projects the tribal revenue is supporting.

**Staff Recommendation:** Approve the April Finance letter that requests the revised budget bill language and directs the tribal revenue to the State Highway Account.



**11. Public Safety Radio (BCP #5).** The Department requests funding of \$7.2 million in 2007-08 and a total of \$19.6 million over five years, to convert the low band radio systems concentrated in the mountainous regions of District 10 (east of Stockton) to a high band system. The Department indicates that most Caltrans Districts (3, 4, 6, 7, 8, 9, 11, and 12) currently operate on high band, but four districts (1, 2, 5, and 10) still operate on low band. The Budget Change Proposal does not address the Administration's plans for the other Districts that operate with low band. Additional information provided by the Department suggests the total cost of upgrading radio systems in all four districts that operate currently on low band would be in the range of \$50 million.

**Background / Detail:** This issue was heard by the Subcommittee at the March 29, 2007 hearing and rejected. One factor in the rejection was that the Office of Emergency Services (OES), which chairs the Public Safety Radio Strategic Planning Committee (PSRSPC), had not released the annual Statewide Integrated Public Safety Communications Strategic Plan that was due January 1, 2007. The OES has since released the plan and it was discussed at subsequent Subcommittee hearings on April 11 and May 10. At the May 10 hearing, Caltrans Director Will Kempton requested the Subcommittee reconsider the Caltrans proposal now that the OES plan has been submitted and discussed in the Subcommittee.

**Staff Comment:** The Caltrans proposal was discussed at the May 10 hearing in the context of the California Highway Patrol (CHP) ongoing radio project and the PSRSPC plan for radio interoperability. The Caltrans proposal is narrowly focused on highway corridors and does not attempt to add broad geographic coverage like the CHP system. Due to the limited scope, the Caltrans system is less expensive. The project would include updated portable and mobile equipment that would improve interoperability with the CHP and other public safety entities.

**Staff Recommendation:** Rescind the prior vote and approve the Caltrans radio request.

**12. Corridor System Management Plan (May Revision Finance Letter):** The Administration requests a two-year appropriation of \$9.67 million, \$4.888 million in 2007-08 and \$4.78 million in 2008-09, for contracting costs associated with the development of corridor system management plans. Caltrans proposes to develop a plan for each of the corridors in which a Corridor Mobility Improvement Account (CMIA) project has been funded. Specifically, the funds would be used to develop micro-simulation models of each corridor.

**LAO Recommendation:** The Legislative Analyst recommends the Legislature provide only a single year appropriation of \$4.888 million and adopt SRL to report on progress of proposed work and its benefits.

There is a current-year appropriation of \$5 million for the first phase of the micro-simulation project to identify and simulate strategies to manage certain traffic corridors for congestion. Discussions with the department indicate that due to delays this first phase has not yet been implemented and contracts will not be awarded for the computer simulation efforts until the end of May. Given this progress (or lack of progress), it is unlikely that the department will award contracts for the full amount requested for the next two fiscal years. Depending on progress, the Legislature can appropriate the requested \$4.78 million for 2008-09 in the 2008-09 budget.

**LAO Supplemental Report Language:**

*By April 1 of 2008, the Department of Transportation shall report to the Joint Legislative Budget Committee, the fiscal subcommittees and policy committees on transportation on its micro-simulation efforts in developing corridor system management plans (CSMP) with funds appropriated in 2006-07, 2007-08 and for the initial pilot project on I-880. The report shall include the following:*

- (1) For each corridor for which a CSMP is to be developed, provide:*
  - The status of the micro-simulation modeling, including the level of completion.*
  - The total cost of the micro-simulation modeling contract.*
- (2) A description of the alternatives to micro-simulation modeling.*
- (3) Comparison of costs and benefits of micro-simulation modeling versus other alternatives in identifying strategies for long-term corridor management.*
- (4) An assessment of the types of corridors that are best suited and least well suited for the use of micro-simulation modeling.*
- (5) A description of the accountability framework developed and the advantages and disadvantages compared to current reporting methods.*

**Staff Recommendation:** Adopt the LAO recommendation – provide one-year funding of \$4.888 million and adopt the suggested Supplemental Report Language.

**13. Bicycle Account Grants (Staff Issue).** The Governor's Budget includes \$5.0 million for local assistance bicycle grants, consistent with the level of funding specified in Street and Highways Code 2106. However, this is \$4.2 million less than 2006-07 funding and \$2.2 million less than 2005-06 funding.

**Background / Detail:** Senate Bill 1772 (Ch 834, St of 2000, Brulte) increased funding for bicycle facility grants from \$3.0 million to \$7.2 million through 2005-06, and then to \$5.0 million in 2006-07 and thereafter. Funding for 2006-07 was \$9.2 million (\$4.2 million more than the statutory level) because multiple years of interest earnings were included in the appropriation. Funding for the Bicycle Account comes from the Highway Users Tax Account. Absent the transfer to the Bicycle Account, the funding would otherwise be transferred to the State Highway Account.

According to the Caltrans website, 27 bicycle projects across the state will receive program funding in 2006-07. Local and other funding sources will match \$9.2 million in Bicycle Account funds for total project expenditures of \$27.3 million. The program is over subscribed.

The following chart provides a history of Bicycle Account appropriations (in millions):

Year	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08*
Appropriation	\$7.2	\$7.2	\$7.2	\$7.2	\$9.2	\$5.0

\*proposed

**Staff Recommendation:** Amend Street and Highway Code Section 2106 to increase annual revenue for the Bicycle Account to \$10 million and increase the budget bill appropriation to \$10 million.

## 2600 California Transportation Commission

The California Transportation Commission (CTC) is responsible for the programming and allocating of funds for the construction of highway, passenger rail, and transit improvements throughout California. The CTC also advises and assists the Secretary of the Business, Transportation and Housing Agency and the Legislature in formulating and evaluating State policies and plans for California's transportation programs.

The January Governor's Budget proposes total expenditures of \$5.7 million and 17.6 positions for the CTC (no General Fund). The April Finance Letter increases the proposed CTC budget by \$584,000 and 5.0 positions.

### Discussion / Vote Issues

- 1. Proposition 1B Workload - New Positions (BCP #1, April FL #1):** The Administration requests \$873,000 (Proposition 1B bond funds) and 7.0 positions to perform workload associated with two components of Prop 1B. The BCP #1 request is \$289,000 and 2.0 positions for the following bond programs: the Corridor Mobility Improvement Account (CMIA) and the Trade Corridor Improvement Fund (TCIF). The April Finance Letter #1 request is \$584,000 and 5.0 positions for the following bond programs: State Transportation Improvement Program, the State Highway Operation and Protection Program, Local Transit, Local Streets and Roads, State-Local Partnership, Grade Separations, State Route 99, and Local Seismic Retrofit.

**LAO Recommendation:** In the February *Analysis of the 2007-08 Budget Bill*, the Legislative Analyst recommended that the CTC be designated by the Legislature to perform ongoing oversight of all bond related activities. The April Finance letter adds additional CTC staff to provide oversight for the bond categories not included in the January Budget, and is consistent with the LAO recommendation.

**Staff Comment:** The following are the estimated costs by bond program:

CMIA:	\$194,000
Trade Corridor:	\$95,000
STIP:	\$220,000
Transit:	\$50,000
State/Local Partnership:	\$111,000
Local Bridge:	\$12,000
Grade Separation:	\$40,000
SHOPP:	\$111,000
Local Streets and Roads:	\$40,000

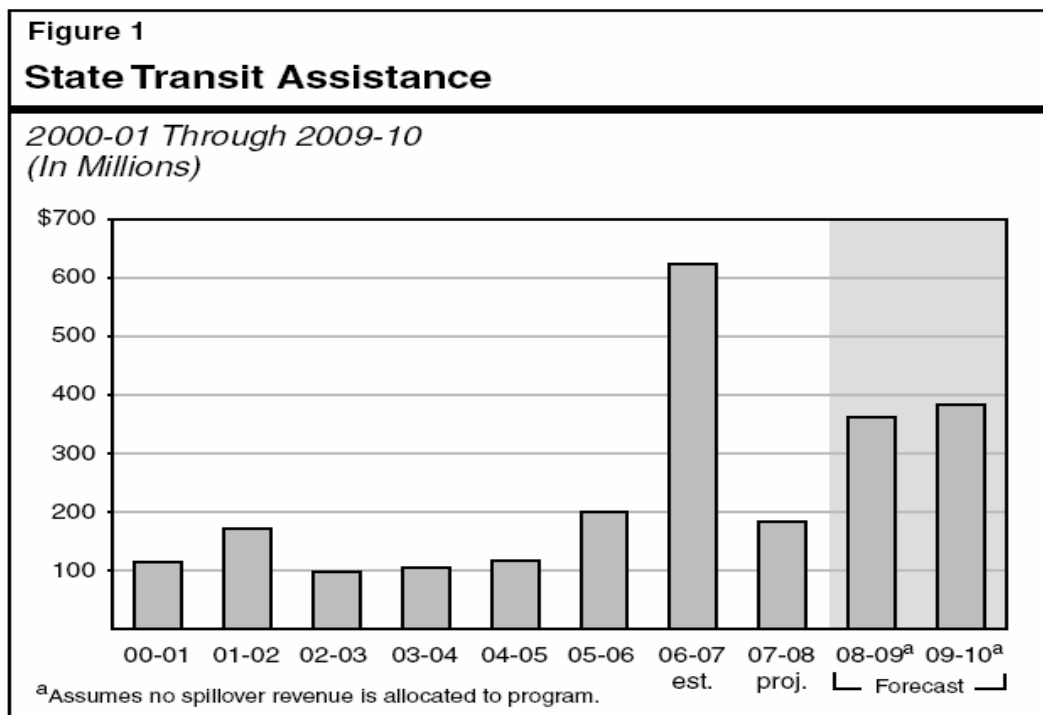
**Staff Recommendation:** Approve the budget request for Prop 1B staffing. Further adjustments may be warranted in the Conference Committee pending the final Prop 1B package.

## 2640 Special Transportation Programs

The State Transit Assistance (STA) budget item provides funding to the State Controller for allocation to regional transportation planning agencies for mass transportation programs. Revenue traditionally comes from the sales tax on diesel fuel and a portion of the sales tax on gasoline (including a Proposition 42 component), and is available for either operations or capital investment. With the passage of the Highway Safety, Traffic Reduction, Air Quality, and Port Security Bond Act of 2006 (Prop 1B), bond funds are also available for this program. However, bond funds may only be used for capital investment.

The Governor's January Budget proposed funding of \$784.7 million for State Transit Assistance – an increase of \$160.9 million. This proposal includes \$600 million in Prop 1B bond funds and \$185 million in traditional fuel sales tax funds. However, this proposal includes trailer bill language that would redirect \$411 million to aid the General Fund (see Caltrans issues #8 earlier in this agenda for a complete discussion of the General Fund proposal). Absent this redirection proposal, current statute would provide for an additional \$411 million for STA. The May Revision retains the overall proposal, but adjusts STA funding up by about \$21 million and redirected funding up by \$98 million – both due to the new fuel sales tax revenue forecast.

The chart below, from the LAO's *Analysis of the 2007-08 Budget Bill*, provides a historical look and future projection of baseline funding for this item (assuming the Governor's January proposals are adopted, and excluding all Proposition 1B bond funds).



**Issue for Discussion / Vote:**

- 1. Shift Spillover Revenue from STA to Education (Gov Budget and May Finance Letter – includes Trailer Bill Language).** The Administration proposes a permanent shift of “spillover” revenue from the STA to the Home to School Transportation Program currently funded as a Proposition 98 General Fund obligation. While the proposed STA budget is up overall, the STP would actually receive a \$508 million (updated for May Revision) cut relative to what current statute dictates. This program, under statute, would receive 50 percent of specified “spillover” gasoline sales tax revenue; which, with the proposed bond revenue and other base revenue, would total \$1.294 billion. The Administration indicates this \$508 million reduction ties to an overpayment of \$95 million in 2006-07 and the STA’s share of 2007-08 spillover revenue, which is estimated at \$413 million. The spillover reduction is proposed to be an ongoing budget reduction and proposed trailer bill language would amend statute to end the transfer of 50 percent of spillover revenue to this item. This proposal is part of the larger Administration proposal to use \$1.3 billion in Public Transportation Account revenues for General Fund relief. The overall proposal is discussed in the Caltrans section (see Caltrans issue #8).

**Staff Comment:** The broader Spillover / Public Transportation Account proposal is an issue in the Caltrans section of this agenda. The action taken for this issue should conform to the action on that issue. Staff concurs with the calculated overpayment of \$95 million in 2006-07. The intent of the 2006 Budget Act was to provide STA 80 percent of specified revenue, not a specified dollar amount, as is described in budget trailer bill SB 1132 (Chapter 56, Statutes of 2006). However, because language in the Budget Bill (AB 1801 and AB 1811) was not amended to reference the changes in SB 1132, the State Controller overpaid the STA in 2006-07 by about \$95 million.

**Staff Recommendation:** Conform to the action taken on the Governor’s proposal to shift \$1.3 billion in PTA funds to General Fund obligations (see Caltrans issue #8). If that proposal was rejected, the conforming action would be to augment the STA budget by \$434 million (\$21 million for the revenue adjustment in the May Revision and \$413 million to add back STA’s statutory share of spillover revenue). Reject the proposed trailer bill language to redirect the spillover revenue, but approve the language to correct for the Controller’s overpayment in 2006-07.

## 2665 High-Speed Rail Authority

The California High-Speed Rail Authority (HSRA) was created by Chapter 796, Statutes of 1996, to direct development and implementation of inter-city high-speed rail service that is fully coordinated with other public transportation services. The total cost to build the entire system was most-recently estimated at \$37 billion.

The January Governor's Budget proposed \$1.2 million and 6.5 positions for the HSRA, a decrease of \$13.2 million and no change in positions. Last year the Legislature augmented the HSRA budget by \$13 million and 3 positions to: (1) complete the draft environmental impact report for the Central Valley to San Francisco Bay Area route; (2) complete a financing plan to be submitted to the Legislature no later than May 1, 2007; and (3) commence site-specific environmental work, right-of-way acquisition, and identification of necessary grade separations to improve and preserve rail corridors. Current law provides for a proposition on the November 2008 ballot to provide \$9.95 billion in general obligation bonds for the high-speed rail and related rail projects; however, the Governor proposes to delay this bond vote indefinitely.

1. **High Speed Rail Project Implementation (Report from HSRA).** The HSRA was provided \$13.0 million in the 2006 Budget Act to begin project implementation, including project-specific environmental work, right-of-way acquisition, and identification of necessary grade separations to improve and preserve rail corridors. In a report to the Legislature dated March 8, 2007, the HSRA indicated that an additional \$103.3 million would be needed in 2007-08 (above the \$1.2 million in the Governor's Budget) to continue implementation of the project. Funding at the \$103.3 million level assumes the state is proceeding to construction of the project, with additional funding to come from the 2008 \$10.0 billion ballot measure or other funding mechanisms. The total cost of the project was most-recently estimated at \$37 billion. The expenditure plan from the HSRA report is outlined in the table below (\$ in thousands):

Description	2006-07 Budget Allocation	2007-08 Budget Request*
Financing Plan	\$750	\$500
Visual Simulation	1,000	750
Program Management	3,094	12,000
Los Angeles - Orange County (Prelim Engr & EIR/EIS)	2,500	4,500
Los Angeles - Palmdale (Prelim Engr & EIR/EIS)	2,600	15,000
Los Angeles - San Diego (Prelim Engr & EIR/EIS)	900	7,000
Palmdale - Fresno (Prelim Engr & EIR/EIS)	1,100	11,000
Fresno - Sacramento (Prelim Engr & EIR/EIS)	500	5,000
San Francisco - Merced (Prelim Engr & EIR/EIS)		10,000
Right-of-Way Purchase		37,000
Land Use Planning	200	100
Program Management Oversight		150
3.0 New HSRA Staff		250
Bay Area - Central Valley "Next-Tier" EIR/EIS	350	
<b>Total</b>	<b>\$12,994</b>	<b>\$103,250</b>

\* Amounts are HSRA Board requests beyond funding included in the Governor's Budget.

**Staff Comment:** As was indicated on the prior page and above, the Financing Plan due May 1, 2007, has been delayed to 2007-08. Therefore, the Subcommittee does not have information on expenditures and funding options beyond 2007-08. However, the table above indicates how the HSRA would continue implementation of the project in 2007-08 if \$103 million in new funding is provided.

**Staff Recommendation:** If the Subcommittee rejected the Governor's proposal to shift \$1.3 billion in PTA funds to General Fund obligations (see Caltrans issue #8), staff recommends using some of this additional Public Transportation Account (PTA) funding to augment the HSRA budget. Augment the HSRA budget by \$40 million (PTA) – this action would put the HSRA into the budget Conference Committee where the level of funding can be further reviewed and budget bill language developed to specify authorized expenditures.



## 2720 California Highway Patrol

The mission of the California Highway Patrol (CHP) is to ensure the safe and efficient flow of traffic on the state's highway system. The CHP also has responsibilities relating to vehicle theft prevention, commercial vehicle inspections, the safe transportation of hazardous materials, and protection and security for State employees and property.

The January Governor Budget proposed \$1.831 billion in total expenditures (no General Fund) and 11,012 positions for the CHP, an increase of \$150.1 million (9 percent) and 325.7 positions.

### Issues Proposed for Discussion and Vote:

- 1. Motor Carrier Safety Program (BCP #7 & Trailer Bill Language / Administration Revisions).** The Governor's Budget requested a permanent increase of \$7.7 million to augment staffing 67.9 positions (60 Motor Carrier Specialists and 11.5 support positions). The Administration indicated this would allow the Department to complete 100 percent of the Biennial Inspection of Terminals (BIT), instead of the current 58 percent inspection rate. Motor Carrier Specialists visit terminals to: (1) inspect maintenance and inspection reports for buses and trucks; (2) inspect a sample of required driver records; and (3) investigate hazardous materials handling practices. The Department indicates that statute requires fees to be set at a level to fund the program; however, currently the Motor Vehicle Account (MVA) subsidizes \$2.1 million of the cost. Trailer bill language is requested to increase fee levels for motor carriers to pay the full program cost.

**LAO Recommendation:** In the *Analysis of the 2007-08 Budget Bill*, the LAO indicates that increased inspections and the move toward self-financing make sense, but that the fee structure is flawed. The LAO recommends that the Administration develop a more rational fee schedule and that only 32 of the requested 71.5 positions be approved.

**March 14, 2007 Hearing.** At the March hearing, the CHP indicated that they were modifying their fee proposal and asked that the Subcommittee keep the issue open.

**Revised CHP Proposal:** The CHP indicates that they have continued to work with industry to address concern about a fair distribution of fees, while also maintaining the amount of revenue necessary to provide for a self-supporting program. The revised fee structure is expected to increase program revenue from the \$8.2 million received in 2005-06 to \$14.8 million in 2007-08 (and to \$18.1 million in 2009-10 and ongoing). The CHP has also revised the schedule to hire new staff, as such the new incumbents are hired at multiple times in 2007-08 and also in 2008-09. The new hiring schedule reduces 2007-08 costs from the \$7.7 million in the Governor's Budget to \$3.4 million in the revised proposal. The existing fee schedule is \$400, except for very small operators that pay \$100. The new proposed fee schedule (table below) provides revised fee groups based on the size of the terminal fleet.

<u>Terminal fleet size</u>	<u>Required fee per terminal</u>
<u>1</u>	<u>\$270</u>
<u>2</u>	<u>\$375</u>
<u>3 to 8</u>	<u>\$510</u>
<u>9 to 15</u>	<u>\$615</u>
<u>16 to 25</u>	<u>\$850</u>
<u>26 to 50</u>	<u>\$1,040</u>
<u>51 to 90</u>	<u>\$1,165</u>
<u>91 or more</u>	<u>\$1,870</u>

In addition to the fees outlined above, the motor carrier shall submit an additional \$350 for each of their terminals not previously inspected under this program.

**Staff Recommendation:** Approve the revised funding, staffing, and fee levels, including the adoption of revised trailer bill language.

- 2. CHP's Enhanced Radio System (May Finance Letter).** The Governor's January Budget includes \$108 million for the 2007-08 cost of upgrading the CHP's public safety radio system. Last year, the Legislature approved this five-year project that had total costs originally estimated at \$494 million. The project will enhance radio interoperability with other public safety agencies and provide additional radio channels for tactical and emergency operations. As part of last year's project approval, the Legislature required annual project reporting for the life of the project – the first report was due March 1, 2007. The report was submitted in April and indicates some major cost escalations. The report indicates that the CHP intends to down-scope the project instead of requesting additional funds. This revised project proposal was discussed at the May 10 hearing, but action was held pending receipt of the anticipated May Finance Letter. The May Letter requests a reversion of \$16.4 million in 2006-07 funding (from \$56.9 million to \$40.2 million). The CHP also indicates the 2007-08 cost estimates have fallen as a result of the down-scoped project – the 2007-08 budget should be reduced by \$10.3 million (from \$108.0 million to \$97.7 million).

**Staff Comment:** The CHP's annual report and their revised radio plan were discussed extensively at the May 10 hearing. The May Revision Letter to revert some 2006-07 funds and the additional request to adjust 2007-08 funding are consistent with the discussion at the May 10 hearing.

**Staff Recommendation:** Approve the May Finance Letter to revert \$16.4 million in 2006-07 funds, and additionally reduce 2007-08 funding by \$10.3 million to conform to the revised CHP cost estimates.